

FDIC State Profile

Fall 2005

Michigan

Michigan continues to struggle with poor employment and population trends.

- Michigan was the only state reporting year-over-year job losses at second quarter 2005. Manufacturing job losses continue to be the primary drag on Michigan's economy partly because of auto industry cutbacks (see Chart 1). However, sectors such as construction, trade, and finance that previously posted promising employment gains have slowed hiring. Only the lower paying sectors, including leisure and hospitality, government, and educational and health services, continue to show growth.
- Grand Rapids-Wyoming and Kalamazoo-Portage** were the only Michigan metro areas to post job growth in second quarter 2005, adding a combined 1,400 employees to nonfarm payrolls.
- Michigan consumers quickly felt the effects of the recent Gulf Coast hurricanes as higher gas prices took a larger share of their paychecks. Should energy prices remain elevated, some energy-dependent manufacturers (especially auto producers and suppliers) may see profit margins squeezed; farmers may see higher harvest and shipping costs; and, ultimately, consumers may alter their spending and travel habits. Still, other industries associated with building materials, construction, and furniture likely will see demand for their products increase as rebuilding efforts commence in the affected areas.

Michigan's sluggish economy dampens residential and commercial office markets.

- Home price appreciation in Michigan and its metro areas has been well below the national level during the past five years. The combination of weak employment conditions, slow population growth, and steady housing starts prevented homeowners from achieving greater price gains (see Chart 2).
- Detroit** commercial office vacancies remained high because office-using employment growth remained stagnant. At second quarter 2005, downtown office vacancies were 24.1 percent, the highest in the nation, despite tax incentives for companies to operate in the

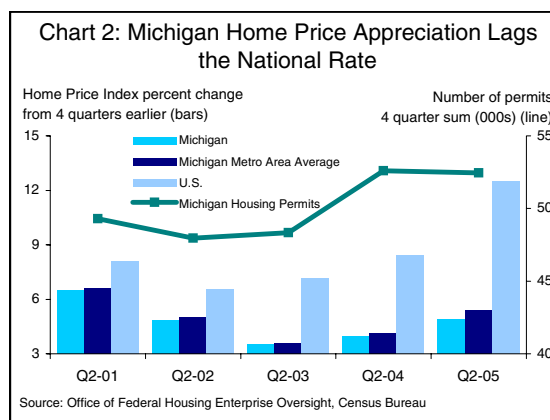
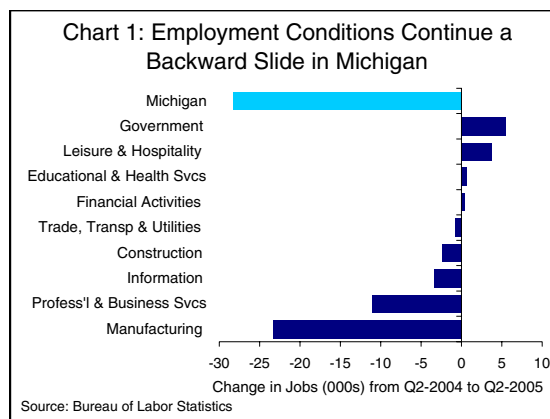


Table 1: Second Quarter Profitability Improves

Income statement contribution (percent of average assets)	3 months ended June 30		Percentage Point Change
	2004	2005	
Net Interest Income	3.67	3.84	0.17
Noninterest Income	1.08	0.97	-0.11
Noninterest Expense	-3.20	-3.18	0.02
Provision Expense	-0.17	-0.19	-0.02
Security Gains & Losses	-0.02	0.00	0.02
Pretax Net Income	1.36	1.44	0.08
Income Taxes	-0.39	-0.41	-0.02
Net Income (ROA)	0.97	1.03	0.06

Source: FDIC. Merger-adjusted data for Michigan's Community Institutions

State Profile

city. Suburban office vacancies were 22.3 percent, also among the highest in the nation.

Employment woes continue to weigh on Michigan households.

- Michigan's per capita personal income growth continued to be among the lowest in the nation with year-over-year growth of 3.3 percent at second quarter 2005, compared to 5.5 percent for the nation.
- Bankruptcies and foreclosures remain elevated and above national levels. The volume of loans in foreclosure was 1.6 percent at first quarter 2005, compared to a national level of 1.1 percent.
- According to data from the Federal Housing Finance Board in the first half of 2005, 29.5 percent of new mortgage loans in the **Detroit-Warren-Flint** metro area contained loan-to-value ratios above 90 percent, compared to a national percentage of 17 percent. In addition, an estimated 33 percent¹ of loans originated in Wayne County in the first half of 2004 were piggyback loans.²

Performance at Michigan's community institutions³ improved despite economic troubles.

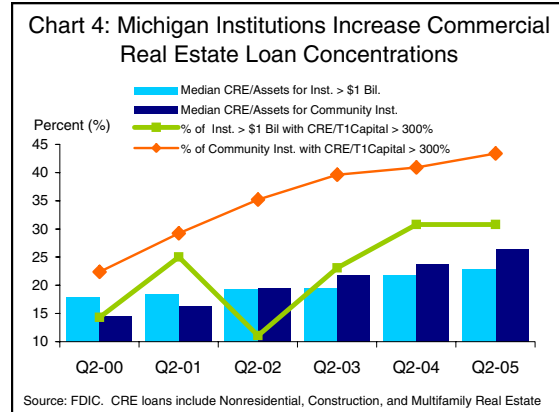
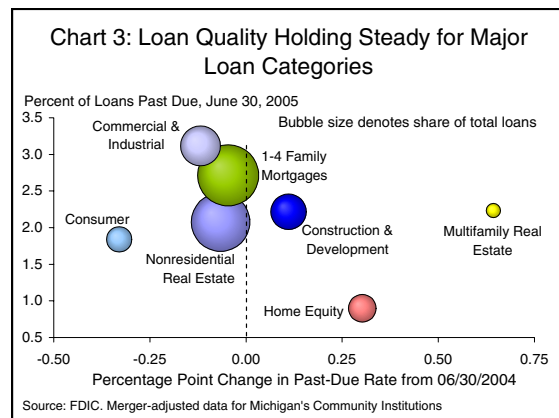
- Return on assets of Michigan community institutions increased slightly from a year ago, buoyed primarily by a significant increase in net interest income and despite a decline in noninterest income and an increase in noninterest expense (see Table 1).
- The net interest margin benefited from an increase in the yield on earning assets that exceeded the increase in the cost of funds. The loan to asset ratio continued to grow, reaching 77.5 percent at second quarter 2005, among the highest in the nation. The majority of the growth came from higher yielding construction and nonresidential real estate lending.

Loan quality improved, but commercial real estate (CRE) exposures warrant close monitoring.

- Past-due and net charge-offs rates at Michigan community institutions declined slightly from a year ago and are moderate at 2.3 percent and 0.2 percent, respectively, at second quarter 2005. Most major loan categories posted declines in past-due rates, with small to moderate increases in home equity, construction, and multifamily real estate

loans (see Chart 3). Loan loss reserve coverage levels declined in line with improving asset quality indicators.

- CRE⁴ lending represents an increasingly important activity for Michigan's community institutions. From June 30, 2000, to June 30, 2005, median CRE loans to total assets increased from 14 percent to 26 percent.
- As of June 30, 2005, 43 percent of Michigan's community banks maintain balances of CRE loans equal to or greater than 300 percent of Tier 1 capital, compared to 22 percent as of June 30, 2000 (see Chart 4).
- A number of Michigan metro areas have shown increasing CRE concentrations among some banks. In the Detroit metro, which has the largest number of institutions, community banks have embraced CRE lending. The percentage of institutions with CRE concentrations of more than 300 percent of Tier 1 capital climbed to 65.6 percent at second quarter 2005, and the median ratio of CRE loans to assets represents a significant 35.7 percent.



¹Charles A. Calhoun, PhD, "The Hidden Risks of Piggyback Lending," June 2005. (Note: data based on a sample of loans).

²Piggyback loans typically involve first and second mortgages originated simultaneously to enable the borrower to receive a larger loan amount requiring a lower down payment.

³Community institutions are insured institutions with less than \$1 billion in assets, excluding new (less than three years old) and specialty banks. Data adjusted for merger activity.

⁴CRE consists of multifamily residential real estate, construction, and nonresidential real estate loans.

Michigan at a Glance

ECONOMIC INDICATORS (Change from year ago, unless noted)

Employment Growth Rates	Q2-05	Q1-05	Q2-04	2004	2003
Total Nonfarm (share of trailing four quarter employment in parentheses)	-0.6%	-0.1%	-0.3%	-0.4%	-1.5%
Manufacturing (16%)	-3.3%	-3.0%	-2.7%	-2.9%	-5.7%
Other (non-manufacturing) Goods-Producing (5%)	-1.0%	1.1%	0.5%	-0.2%	-4.5%
Private Service-Producing (64%)	-0.3%	0.3%	0.3%	0.2%	-0.5%
Government (16%)	0.8%	0.7%	-0.6%	-0.5%	-0.2%
Unemployment Rate (% of labor force)	7.0	7.1	6.9	7.1	7.1

Other Indicators	Q2-05	Q1-05	Q2-04	2004	2003
Personal Income	3.6%	2.9%	1.8%	1.8%	4.9%
Single-Family Home Permits	-7.7%	6.9%	2.5%	1.5%	6.3%
Multifamily Building Permits	21.1%	-13.1%	-24.6%	0.9%	-2.3%
Existing Home Sales	-0.5%	2.9%	3.9%	2.9%	1.9%
Home Price Index	4.9%	5.0%	4.1%	4.5%	3.5%
Bankruptcy Filings per 1000 people (quarterly annualized level)	7.56	7.08	6.39	6.32	6.18

BANKING TRENDS

General Information	Q2-05	Q1-05	Q2-04	2004	2003
Institutions (#)	173	174	176	173	178
Total Assets (in millions)	211,931	206,163	199,714	194,630	196,664
New Institutions (# < 3 years)	4	5	5	4	8
Subchapter S Institutions	12	12	12	12	10

Asset Quality	Q2-05	Q1-05	Q2-04	2004	2003
Past-Due and Nonaccrual Loans / Total Loans (median %)	1.69	1.77	1.81	1.82	2.15
ALLL/Total Loans (median %)	1.21	1.23	1.25	1.24	1.30
ALLL/Noncurrent Loans (median multiple)	1.80	1.81	1.71	1.67	1.41
Net Loan Losses / Total Loans (median %)	0.06	0.04	0.06	0.12	0.14

Capital / Earnings	Q2-05	Q1-05	Q2-04	2004	2003
Tier 1 Leverage (median %)	9.48	9.41	9.29	9.25	9.08
Return on Assets (median %)	1.01	0.98	0.98	0.97	1.10
Pretax Return on Assets (median %)	1.41	1.37	1.35	1.35	1.52
Net Interest Margin (median %)	4.23	4.17	3.98	4.08	4.12
Yield on Earning Assets (median %)	6.19	5.89	5.63	5.72	6.00
Cost of Funding Earning Assets (median %)	1.96	1.80	1.67	1.70	1.99
Provisions to Avg. Assets (median %)	0.13	0.13	0.12	0.15	0.19
Noninterest Income to Avg. Assets (median %)	0.67	0.69	0.75	0.73	0.89
Overhead to Avg. Assets (median %)	3.03	2.99	3.04	2.97	3.12

Liquidity / Sensitivity	Q2-05	Q1-05	Q2-04	2004	2003
Loans to Assets (median %)	76.5	75.8	74.3	76.2	74.0
Noncore Funding to Assets (median %)	21.5	21.0	19.2	20.5	18.6
Long-term Assets to Assets (median %, call filers)	11.4	11.8	12.9	11.7	12.5
Brokered Deposits (number of institutions)	74	72	65	68	63
Brokered Deposits to Assets (median % for those above)	8.8	9.0	7.0	8.6	7.1

Loan Concentrations (median % of Tier 1 Capital)	Q2-05	Q1-05	Q2-04	2004	2003
Commercial and Industrial	90.3	90.5	94.3	88.3	93.4
Commercial Real Estate	259.0	250.1	241.6	255.5	236.9
<i>Construction & Development</i>	52.0	50.3	47.0	51.3	45.9
<i>Multifamily Residential Real Estate</i>	6.4	5.5	5.4	5.1	4.9
<i>Nonresidential Real Estate</i>	190.4	188.0	193.0	186.0	186.8
Residential Real Estate	277.4	279.2	278.4	272.5	287.2
Consumer	34.6	34.0	37.2	36.1	39.6
Agriculture	2.8	3.0	3.1	3.0	3.5

BANKING PROFILE

Largest Deposit Markets	Institutions in Market	Deposits (\$ millions)	Asset Distribution	Institutions
Detroit-Warren-Livonia, MI	56	76,201	< \$250 million	116 (67.1%)
Grand Rapids-Wyoming, MI	31	10,940	\$250 million to \$1 billion	44 (25.4%)
Lansing-East Lansing, MI	25	4,926	\$1 billion to \$10 billion	9 (5.2%)
Ann Arbor, MI	17	4,445	> \$10 billion	4 (2.3%)
Flint, MI	13	3,782		